

Discussion Paper for the Foundation for the Rights of Future Generations - The housing crisis as a problem of intergenerational justice: the case of Germany

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Veröffentlichungsversion / Published Version
Zeitschriftenartikel / journal article

Empfohlene Zitierung / Suggested Citation:

Lutz, E. (2020). Discussion Paper for the Foundation for the Rights of Future Generations - The housing crisis as a problem of intergenerational justice: the case of Germany. *Intergenerational Justice Review*, 6(1), 24-30. <https://doi.org/10.24357/igjr.6.1.796>

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Discussion Paper for the Foundation for the Rights of Future Generations

The housing crisis as a problem of intergenerational justice: The case of Germany

by Elena Lutz

Executive summary

In this discussion paper, it is shown that the current housing affordability crisis in Germany is a problem of intergenerational injustice since it affects young Germans disproportionately negatively. To address these injustices, the following policy measures are suggested.

1. Policies to assure affordable rents

- a. *Rent controls*: Well-designed rent controls help keep rent-price increases in re-lettings in check, while still allowing landlords to pass renovation costs on to their renters and to increase their rents by a small percentage annually. This would especially benefit young individuals, since the young move more often than baby boomers and are therefore disproportionately negatively affected by price increases in re-lettings.
- b. *Strengthening social housing*: Local, state, and national governments must invest in the provision of social housing to provide below-market-priced housing for the most vulnerable households. This measure is especially important in large cities, where rents have risen steeply over the past decade, threatening to displace many poor households.

2. Measures to facilitate first-time homeownership for young Germans.

Supporting young adults in becoming first-time homeowners is another important area in which public policy can help mitigate the negative effects of the housing crisis for young Germans. This can be achieved via:

- a. *First-time home buyer programmes*: First-time home buyer programmes support individuals who are buying their first home through grants or other financial stimuli, such as a first-time home buyer tax credit. Several countries, such as Australia or Canada, already have such programmes in place, helping young individuals to become homeowners. Such measures could also be adopted in Germany.
- b. *Access to credit for first-time buyers*: Young people often face credit constraints when buying their first home since they do not yet own a home they could use as collateral. Governmental programmes, such as the first-time homebuyers plan

in Canada, can help young individuals to obtain resources for the down payment on a mortgage, thereby improving their chances to be able to obtain a mortgage at a reasonable interest rate.

3. Measures to increase housing supply.

To address issues of housing affordability and intergenerational justice, public policy should aim to increase the housing stock. It should also provide for the needs of young generations, especially in urban areas. Concrete measures to achieve these goals include:

- a. *Densification policies*: Densification policies consist of relaxing zoning restrictions. This allows landowners to build more densely and taller, thereby increasing the overall housing supply. Relaxing zoning restrictions allows the housing supply to respond to an increased demand and can therefore prevent house prices from rising. Therefore, densification policies have become a widespread tool to address housing unaffordability and could be used more extensively in German cities.
- b. *Using existing housing stock more efficiently*: Another factor that hinders young people from finding adequate homes is that houses that could be occupied by a young family or multiple students are often occupied by an old couple or individual who continue living in the homes where they raised their children, even after the children have moved out. Online platforms, such as *Tauschbörse*, that connect young individuals currently living in a smaller property with older people currently living in a larger property can help in using the existing housing stock more efficiently.

Since the current German housing crisis is a predominantly urban phenomenon, Germany's large cities should be the primary focus of these policies. Yet, because of architectural and socio-economic differences between and within cities, there exists no one-size-fits-all solution. Nevertheless, the above measures can serve as a starting point for developing comprehensive measures to fight intergenerational injustice in the German housing market.

Introduction

The majority of high-income countries are currently experiencing an unprecedented housing affordability crisis. Over the past two decades, housing costs have skyrocketed with house-price growth clearly outpacing growth in real wages. As a result, more and more households are struggling to afford adequate housing

in a suitable location – a phenomenon commonly known as “the housing affordability crisis”. Its tangible consequences are a rising number of households that face burdensome housing costs (defined as having to spend more than 40% of their income on housing), decreased satisfaction with their housing situation for many households, as well as increasing numbers of homeless in

some of the world's wealthiest nations (Eurostat 2020a). However, not all social groups are equally affected by the current housing crisis: numerous studies, such as Fields and Hodgkinson (2018), document that individuals from the lower end of the income distribution suffer the most from the housing crisis. For instance, in Germany 49.5% of households with incomes below 60% of the median income experience burdensome housing costs, i.e. they spend more than 40% of their disposable income on rent, compared to only 7.5% of households above 60% of the median income (Eurostat 2020b). Thus, many scholars and politicians have pointed out that the current housing affordability crisis creates severe social injustice in the housing market.

Yet, the key argument of this paper is that the current housing crisis is not only a problem of injustice towards the poor, but also a crisis of intergenerational justice: evidence shows that younger generations are more adversely affected by the housing crisis than individuals from the baby boomer generation (Arundel 2017, Flynn 2020). For instance, young individuals today are less likely to be able to afford to buy a home than the generation of their parents was at their age (Ball 2016, Market 2017). This is because the price of a house relative to a worker's annual wage has increased drastically over the past decades, making it very difficult for young people to become homeowners. Second, young people also struggle to pay their rent more often and live more often in overcrowded housing.

The current housing crisis is a double-edged sword. On the one hand, those individuals that do not (yet) own a home suffer from the housing crisis: for them, increasing house prices result in higher rents they must pay to their landlords and a lower likelihood that they can afford to become homeowners themselves (Haurin et al. 2007). On the other hand, there is a section of the population that benefits from the current house-price increase: homeowners. Their houses have gained in value, meaning that they can resell their homes at a much higher price than the price at which they acquired them, or that they can ask for higher rents. Tax breaks on homeownership and favourable credit conditions arising from being able to use a house as collateral further deepen this insider-outsider dynamic (see Ball 2016). Since older individuals are much more likely to own a home than individuals from younger generations, older generations tend to benefit from the current housing crisis while millennials suffer from it, naturally pitting the young against the old (Fuller et al. 2020).

Against this backdrop, this discussion paper asks the following questions: Does the housing affordability crisis constitute a problem of intergenerational injustice? And if so, which policies would be most effective in improving the situation of young people in the housing market?

This discussion paper examines the case of Germany. In many respects, Germany is representative of the situation in other high-income countries such as France, the UK, Canada, or the US: housing prices and rents have risen steeply in the country's large cities, posing serious problems to housing affordability. The German housing crisis therefore is a predominantly urban phenomenon, which is similar to the situation in other countries. Yet the German housing market differs from other countries in certain aspects. First, while Germany has experienced steep house price increases, these increases are less than in other countries, such as in the UK or Spain. Second and most importantly, Germany has a higher share of renters in international compari-

son, e.g. to Northern America or Southern Europe. For instance, the homeownership rate in Germany in 2018 was 51.5% compared to 65.1% in the UK, 72.4% in Italy, and 96.4% in Romania (Statista 2020). In Germany, renting is socially accepted and thus not only a housing tenure for low-income households that lack other options. Therefore, German renters also enjoy more comprehensive rights than in other countries (Voigtländer 2009). German housing policy must thus focus more strongly on the rental sector than in other countries. This German peculiarity should also be kept in mind when generalising the policy recommendations of this study. However, homeownership rates are currently declining in many countries such as the US and the UK, meaning that more countries may converge to the German level of homeownership in the future.

The remainder of this paper is organised as follows. First, I describe the extent of the housing crisis in Germany, then I show in detail how younger generations are more adversely affected by the housing crisis than older generations and examine the causes of this. I end by proposing different policies that could help to improve the situation of younger generations in the housing market, thereby addressing the issue of intergenerational justice in the field of housing.

The housing crisis in Germany

As in many other countries, Germany has experienced big increases in house prices and rents. House prices started to rise in 2012 and have risen very sharply since. In fact, over the past eight years German house prices have risen as much as during the 45 years between 1975 and 2010, and they have now even surpassed their pre-2008 crisis highs, which is also the case in e.g. the UK and the US. Furthermore, rents have also risen steeply. This is particularly important in the German case as Germany is a "nation of renters", with lower homeownership rates than other countries (Voigtländer 2009). Yet, at the heart of the current housing affordability crisis lies not only the problem of rising house prices, but also the problem that wages have not risen at the same pace as house prices. For instance, in Germany the price of an average flat has risen by 60% over the past 10 years while the average wage has only risen from US\$44,000 in 2008 to US\$49,800 in 2018, which corresponds to an increase of 13.8% (OECD 2020a, RWI 2019). Since house prices have risen so much faster than wages, housing has become less affordable for a majority of the population.

However, it is important to note that not all regions in Germany are equally affected by the housing crisis: large urban areas, such as Munich or Berlin, are by far the most strongly affected (Glaeser and Ward 2009). For instance, in Munich apartment prices have risen by approximately 240% compared to the national average of 60% (RWI 2019). Unsurprisingly, individuals living in large cities report that finding adequate housing is extremely difficult (European Commission 2015). According to a survey conducted by the European Union, 96% of Munich's population say finding adequate housing at a reasonable price is very hard (European Commission 2015). These values are among the highest of all European cities (ibid.). Besides large metropolitan areas such as Munich, Berlin, or Hamburg, also smaller towns with a strong job-market or large universities experienced steep price increases (Felhberg and Miessner 2015) while many rural regions have not experienced a housing crisis at all, and house prices have even

declined in some areas (Fuest and Immel 2019). Thus, when discussing the German housing crisis and potential policies to mitigate it, it is important to note that the housing crisis occurs only in certain areas of Germany and that there is no one-size-fits-all solution.

The consequences of the German housing crisis are further exacerbated by a decline in the stock of social housing in Germany over the decades preceding the current housing crisis. A key function of social housing is to provide relief for households that are unable to afford rent. Yet the market share of social housing has steadily declined in most advanced countries (Whitehead and Scanlon 2007). This also holds true for Germany, where local governments – for instance in the city of Munich – sold large parts of their social housing stock to private investors. The share of social housing in the total of housing in Germany has declined by almost 75% over the past 30 years, from 4% in 1987 to 1.2% in 2017 (Deutscher Gewerkschaftsbund 2020). Especially in large cities such as Berlin or Munich, this leaves local governments with few options to provide housing for those households that are unable to find housing through the general housing market. Thus, the decline in social housing aggravates the housing market situation in German cities.

The German housing crisis: A problem of intergenerational justice?

The key argument of this paper is that the current German housing crisis affects younger generations more adversely than older generations. This argument is based on a large body of research that documents the differing effects of house prices on different generations (see Arundel 2017, Fuller et al. 2020, Flynn 2020, McKee 2012). For instance, in their recent study covering Germany and other Western European countries Fuller et al. (2020: 314 f.) find that “housing prices’ impact on wealth may have the potential to exacerbate cleavages between older and younger generations. Homeownership rates for millennials are steadily declining, not only because their disposable income cannot keep pace with housing prices, but also because they have higher (student) debt burdens than their parents when they first attempt to climb the property ladder” – a fact confirmed by Flynn (2020), who shows that homeownership rates among 25–34-year-olds in Germany declined by over one-third from the late 1970s to early 2010s. Higher house prices also mean that millennials remain in their childhood home for a longer period of time. The proportion of Germans aged between 25 and 34 living away from their childhood home dropped by 9.5 percentage points between 1978 and 2015, from 92.7% to 83.3% (Flynn 2020). Thus, the consequences of the current housing affordability crisis are felt more directly by the young.

The main reason why the current housing crisis constitutes a problem of intergenerational justice is that the current house price increases in urban centres lower young individuals’ prospects of becoming homeowners. Given these strong price increases, Inchauste et al. (2018: 17) note that “young people and newcomers are especially affected, while older generations owning homes in prime locations have benefited from significant increases in the value of their capita”. While buying a home has always been costly and difficult for the young, empirical evidence shows that buying a home is more difficult for millennials today than it was for the baby boomer generation back in the late 1970s to the early 1990s.

In Germany, the rate of homeownership among individuals aged 30–39 declined from 10% in 1990 to 2% in 2015 (Marek 2017). But homeownership in the general population increased from 22% to 28% over the same time-period (Marek 2017). The inability to buy a home keeps millennials from participating in the “game” of gaining wealth from quickly-rising house asset prices. Thus, the housing crisis diminishes the opportunities for young individuals to participate in the housing market.

The inequality between younger and older generations is further amplified by the considerable financial advantages for homeowners in Germany. These financial advantages come in the form of better borrowing conditions and tax breaks. First, older households that already own their home can use it as collateral when borrowing. By contrast, young people today who wish to buy a home face severe credit constraints (Marek 2017). They often pay higher interest rates since they do not yet possess a house that they can use as collateral (Carozzi 2019). This creates a vicious circle in which young individuals are unable to become first-time homeowners simply because they do not already own a home. Thus we observe a “growing ability of existing homeowners to raise their housing consumption and outbid others from the available stock” (Ball 2016: 185). Second, tax benefits for homeowners further benefit older people who are more likely to own their own home (Poterba and Sinai 2007). Even though tax benefits for homeownership are less pronounced in Germany than e.g. in the Netherlands or the UK, the German tax system nevertheless favours those living in owner-occupied housing, which means that younger generations that have to rent their homes are often at a disadvantage (Voigtländer 2007). In sum, credit constraints and tax benefits in Germany give rise to an insider-outsider dynamic between the young “Generation Rent” and the older “Generation Landlord”.

The current housing crisis also concerns intergenerational justice in that homeowners are able to pass their assets on to their offspring. As noted by Helbrecht (2019), the opportunities for German millennials to become homeowners increasingly depend on the wealth of their parents, since houses have become so expensive that only those young individuals who receive financial help from their parents can buy their own home (Öst 2011, McKee 2012, Flynn 2020). The housing crisis has led to an increasing re-familialisation of the welfare state, with young adults having to rely more on their parents by e.g. living longer in their parents’ home or by tapping the “bank of mum and dad” when wanting to buy a home (Flynn 2020, p. 323). While many lower or middle class baby boomers were able to buy a home and “climb up the housing ladder”, today only young adults from wealthy family backgrounds can buy a home (Flynn and Schwartz 2017). This dynamic aggravates the already poor social mobility in German society and further exacerbates existing wealth inequality (Fuller et al. 2020). The current housing crisis thus undermines social mobility today and will make society more unequal tomorrow. In sum, the current housing crisis is both a problem of intra- and intergenerational justice, pitting poor against rich and young against old.

Addressing the challenge of intergenerational justice in the German housing crisis

The previous section shows that the current housing crisis engenders marked injustices between younger and older generations.

But what is so problematic about these injustices? Do we really need policies that specifically help younger generations in the housing market? This paper argues that, yes, we do require policies to restore intergenerational justice in the German housing market. If left unaddressed, young generations' raw deal in the housing market will lower economic growth and undermine social cohesion in Germany.

First, young Germans' precarious place in the housing market will negatively impact economic growth: skyrocketing house prices in cities such as Munich or Frankfurt deter young individuals from moving to places where they could find a well-paid job. The dramatically increasing rents in small university towns, such as Tübingen or Göttingen, are another problem particular to Germany (Fehlberg and Mießner 2015). These may prevent young Germans from moving for study. Letting high housing costs deter young people from moving to where they could obtain a productive job and a good education has a negative effect on economic growth (Ortalo-Magné and Rady 2002).

Second, intergenerational injustices in the housing market damage social cohesion. The housing crisis divides the German population into two different groups – richer homeowners and their inheritors versus poorer renters – whose political interests oppose each other. This may give rise to political conflict (Fuller et al. 2020). Furthermore, studies show that many young people are dissatisfied with the government because of their disadvantaged position in the housing market. This undermines the trust of younger generations in their own government (Hoolachan and McKee 2019). There are not only normative motivations for pursuing (intergenerational) justice, there are also very practical reasons that make intergenerational justice in the German housing market an important policy goal.

Policy proposals

There are two broad policy goals through which governments can improve the situation of young Germans on the housing market: policies to *facilitate first-time homeownership* and policies to *increase the supply of affordable housing*.

1. Facilitating first-time homeownership

Supporting young adults in becoming first-time homeowners is one important area in which public policy can help mitigate the negative effects of the housing crisis for young Germans. Purchasing the first small house or apartment – stepping onto the first rung of the “housing ladder” – is an important step which enables young people to be on an equal footing with existing homeowners from the baby boomer generation. Concrete measures to support first-time homeownership include:

- a. First-time home buyer programmes: First-time home buyer programmes support individuals who are buying their first home through grants or other financial stimuli. Several countries, such as Australia or Canada, already have such programmes in place. In Australia, for instance, first-time home buyers receive a grant of A\$7000 from the government (Milligan and Pinnegar 2010). The Canadian government has also initiated a host of measures that facilitate first-time homeownership. These measures include a first-time home buyer tax credit (where first-time buyers pay less tax), a first-time home buyers' plan (through which first-time

buyers can borrow up to CA\$25,000 tax free), and in some states also a land transfer tax rebate (where first-time buyers do not have to pay the land transfer tax) (Government of Canada 2020). Such measures could also be adopted in Germany.

- b. Access to credit for first-time buyers: As stated by Flynn (2020: 321), “governments that create accessible and liquid credit markets make it easier for young people to launch from their parental home”. However, especially since the financial crisis, young people often face severe credit constraints when applying for a mortgage to buy their first home since they do not yet own a home they can use as collateral (Ortalo-Magné and Rady 2002). In this situation, governmental programmes such as the first-time homebuyers plan in Canada could help young individuals to obtain the money for the down payment on a mortgage, thereby improving their chances to be able to obtain a mortgage at a reasonable interest rate.

2. Create more housing that is affordable and meets the younger generations' needs

A second crucial policy area to improve the housing situation of young Germans is to create more affordable housing in urban areas, so that young people can move to booming cities and university towns. Moreover, creating more affordable housing would not only benefit millennials but all German citizens facing burdensome housing costs. The design of social housing units should also take account of the needs of younger generations who tend to marry later and have fewer children and therefore often look for smaller apartments than baby boomers. Concrete measures to achieve these goals include:

- a. Densification policies to increase the housing supply: Home prices have skyrocketed partly because there is a shortage of housing in booming areas such as Munich, Frankfurt and Berlin (Glaeser and Ward 2009). One reason for the current shortage of housing in places where the demand for housing is very high is regulations that restrict building (Glaeser and Ward 2009, Cheung et al. 2009). In Germany, investors must obey strict planning laws that regulate, for instance, how high and how densely investors may build on a certain piece of land. These drive up house prices by restricting supply (Glaeser and Ward 2009, Cheung et al. 2009). Many local governments in larger cities, such as Zürich or London, have realised this problem. Their response has been so-called “densification policies”, which refer to a loosening of current building regulations, allowing investors to build more housing more densely. Such policies may prevent housing prices from rising further, thereby lowering the housing cost burden for the inhabitants of German cities. However, simply allowing for more construction will not be enough, since the price decreases achieved by relaxing building regulations are not large enough to also be felt by poor households (Beer et al. 2007, Freemark 2019). Policies should therefore also aim to produce affordable housing to support the young and the poor, which could be achieved by setting a required minimal percentage of affordable housing in new building projects – a measure called inclusionary zoning (see Schuetz et al. 2009 for more detailed information).

- b. Using existing housing stock more efficiently: Another factor that hinders young people from being able to find adequate homes is the fact that large apartments or houses that could be occupied by a young family or multiple students are often occupied by an old couple or individual. This is because many older couples continue living in the homes where they raised their children, even after their children have moved out. These older individuals may not need nor want their large homes any more but they are now unable to find a smaller flat at a decent price since housing prices have risen so much and – in the case of rented accommodation – they are better off staying with their current rental contract. Platforms exist that connect young people with a smaller property and older people with a larger property, allowing them to switch properties without fees to brokers. An example of this is the German online platform *Tauschbörse*, where two parties can switch their apartments. Of course it is important to ensure that any switching occurs on a voluntary basis and that especially elderly participants are protected from fraud. Nevertheless, a well-designed switching-platform could help in the effort to ensure that the existing housing stock is used more efficiently.
- c. Strengthening social housing: With skyrocketing house prices in many German cities, it is imperative to create housing that also the poor and the young can afford. Social housing, i.e. housing administered by the state or other bodies and rented at below-market price, plays a crucial role in providing affordable housing in Germany as well as in other high-income countries (Scanlon et al. 2015). However, the stock of social housing in Germany has declined substantially in recent years and can no longer meet the rising demand of young and poor individuals (Deutscher Gewerkschaftsbund 2020). For instance, last year the city of Munich received over 30,000 applications for social housing, but it had only approximately 3,500 apartments available (Bayerischer Rundfunk 2020); sometimes, even families or individuals with a disability cannot receive social housing. The situation is similarly precarious in other large German cities. Thus, local, state, and national governments must invest more in social housing. Furthermore, rethinking housing as a right and not a commodity could help achieve this goal: while every German has the right to emergency shelter in case of homelessness, Germans have no legal right to more permanent accommodation, i.e. long-term social housing at affordable rents. Introducing the right to one's own apartment – i.e. a right to social housing for those who need it – could help to hold governments accountable for their social housing policies.
- d. Rent controls: Rent controls are another important measure to ensure the affordability of housing. Targeting rents is an especially important measure in Germany because of the high proportion of households that rent. The German Federal Government enacted such a measure in 2015, the so-called “*Mietpreisbremse*” (literally, “rent-price brake”). It is important to note, first, that the German rent control differs fundamentally from rent controls enacted e.g. in the US: in Germany, rent control does not cap prices but only prevents landlords from drastically increasing their rents. Second, the rent control allows landlords to pass certain costs of improvements to the apartment on to their renters and is therefore unlikely

to discourage investment in the housing stock. Rent controls clearly benefit young individuals since the young move more often than baby boomers who have already settled down in a certain property. Baby boomers are often thus sheltered from drastic rent increases since landlords tend to increase the rent the most when re-letting the apartment rather than for existing tenants. However, first studies on the effect of the *Mietpreisbremse* show that rents in Germany are not decreasing. A reason for this may be its poor enforcement (see Mense et al. 2019). The German government should therefore aim at the proper enforcement of rent controls to improve the situation for young people.

Conclusion

This discussion paper asked whether the German housing market constitutes a problem of intergenerational justice. The analysis showed that individuals from younger generations in Germany are indeed disadvantaged compared to their parents' generation. Soaring house prices have made it impossible for most millennials to buy property as their parents did at their age. Tax benefits and favourable credit conditions for today's homeowners have further excluded millennials from the housing market. The housing affordability crisis also increases inequality within younger generations because many young people's only possibility of becoming homeowners themselves – and therefore of benefiting from rising property prices – is to receive financial support from their parents. Those millennials with wealthy parents are significantly more likely to become homeowners themselves and thus able to profit from price increases. However, millennials – even from the middle class – will most likely never become homeowners if their parents do not have the financial means to support them. Yet, besides ownership, there is also the problem that many young individuals are currently deterred by high housing costs from moving to Germany's most thriving cities such as Munich or Frankfurt in order to pursue their career and education. The ways in which young Germans today are disadvantaged in the housing market call for policies that specifically address the issue of intergenerational justice.

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